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IN THE

Supreme Court of the United States

October Term, 1953

No. 39

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.*, individually and doing business under the firm name and style of HAYDEN, STONE & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, *ET AL.*

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HAVEN B. PAGE,

Defendant.

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, *ET AL.*

Opinions Below

The opinion of the United States District Court (23-32)* is reported in 107 F. Supp. 75. The opinion of the United States Court of Appeals for the Second Circuit (40-52) is reported in 201 F. 2d 439.

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* Unless otherwise stated, references in parentheses are to pages of the record.

Jurisdiction

The jurisdiction of this Court is invoked under 28 U. S. C. §1254. The judgment of the Court of Appeals was entered on January 15, 1953 (52). Petition for a writ of certiorari was filed on April 14, 1953 and granted on June 1, 1953. 345 U. S. 969.

Questions Presented

1. In a civil action for damages under Section 12(2) of the Securities Act of 1933 (15 U. S. C. §77 l (2)) was it error for the Court of Appeals to direct, pursuant to Section 3 of the Federal Arbitration Act (9 U. S. C. §3), the enforcement of the parties' agreement to submit their controversy to arbitration?

2. Did the Securities Act of 1933 repeal by implication the Federal Arbitration Act of 1925 as to investors and as to contracts for the purchase and sale of securities?

Statutes Involved

The pertinent provisions of the Securities Act of 1933 are set forth in the brief of the Securities and Exchange Commission. With respect to the Federal Arbitration Act, however, that brief sets forth only Sections 3 and 10, and predicates, upon the language of Section 3, an argument that "the arbitration statute is applicable only to controversies which are properly 'referable to arbitration'" (SEC Br. pp. 12, 26). But this ignores Sections 1 and 2 of the Act which define its coverage and make it universally applicable, excepting only employment contracts.

Sections 1 and 2 of the Federal Arbitration Act (9 U. S. C.) provide as follows:

"§1. 'Maritime transactions' and 'commerce' defined; exceptions to operation of title

"'Maritime transactions', as herein defined, means charter parties, bills of lading of water carriers, agreements relating to wharfage, supplies furnished vessels or repairs to vessels, collisions, or any other matters in foreign commerce which, if the subject of controversy, would be embraced within admiralty jurisdiction; 'commerce', as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce. July 30, 1947, c. 392, §1, 61 Stat. 670."

"§2. Validity, irrevocability, and enforcement of agreements to arbitrate

"A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such

grounds as exist at law or in equity for the revocation of any contract. July 30, 1947, c. 392, §2, 61 Stat. 670."

Statement of the Case

Petitioner is a citizen of the State of New York (2). Respondents are a partnership doing business in New York under the name Hayden, Stone & Co. (7). They are stock-brokers and dealers in securities and with reference to the transactions herein are subject to the Securities Act of 1933. Petitioner brought suit against respondents and another defendant (not involved here) for damages of $3,888.88 under Section 12(2) of the Securities Act of 1933. His complaint (2-4) alleges in substance that on or about January 17, 1951, respondents sold to petitioner 1,600 shares of the common stock of Air Associates, Incorporated, a New Jersey corporation, and that petitioner paid respondent $29,517.54 therefor. The complaint further alleges that said sale was made by means of certain instrumentalities of transportation and communication in interstate commerce and that it

> "was made by means of communications by the defendants to the plaintiff which were and, which included untrue statements of material facts and omitted to state material facts necessary in order to make the statements made in the light of the circumstances under which they were made, not misleading" (Bar. Fifth; 3).

The complaint further alleges that petitioner did not know that the alleged statements were untrue at the time of his purchase of the stock and that petitioner later sold the stock at a loss of $3,888.88.

The transaction between petitioner and respondents was controlled by the terms and conditions of Margin Agreements duly executed by petitioner dated May 2, 1950 and January 18, 1951 (8-9). The agreement of May 2, 1950 opened a separate account in the name of Anthony Wilko and Mary Wilko (16). The agreement of January 18, 1951 opened a separate account in the name of Anthony Wilko alone (22). The agreements were otherwise identical (43 n. 4). The transaction which is the subject of the complaint in this action took place on January 17, 1951 in the joint account. The last paragraph of these agreements, which was directly above the place for petitioner's signature and was in the same size type as the rest of the agreement, provided:

> "Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators" (16, 22).

The Court of Appeals noted that petitioner made no claim of "fraud or coercion in procuring his signature to the agreement" (44).

Before answering the complaint, respondents moved (5-6), pursuant to section 3 of the Federal Arbitration Act, 9 U. S. C. §3, for an order staying all proceedings in the

action until an arbitration had been had in accordance with the arbitration provision quoted above. Respondents' motion was made upon the complaint, the affidavit of Sherman M. Bijur, a partner of Hayden, Stone & Co. (7-10), and copies of the margin agreements involved (11-22). These constituted the whole record; petitioner submitted no opposing affidavit (43).

The District Court denied the motion, because it did not "feel that arbitration of the issues at bar is consistent with the policy and language as expressed by Congress in the Securities Act" (32).

The Court of Appeals for the Second Circuit reversed (Judge Clark dissenting). Chief Judge Swan wrote an opinion, in which Judge Chase concurred, holding that "we do not find in the purpose or in the language of the statute, any policy argument strong enough to override the policy of the Arbitration Act" (49). The court also held that the margin agreement was subject to the Securities Act of 1933 and "consequently the arbitrators are bound to decide in accordance with the provisions of section 12(2)" and that "Failure to do so would * * * constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (48, 49).

SUMMARY OF ARGUMENT

Both the Federal Arbitration Act of 1925 and the Securities Act of 1933 establish important policies of Congress and accomplish important purposes.

"The purpose of that Act [the Federal Arbitration Act] was deliberately to alter the judicial atmosphere pre-

viously existing" which was hostile to arbitration. *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F. 2d 978, 985 (2d Cir. 1942). It establishes that "A written provision in * * * a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction * * * shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Section 2, 9 U. S. C. §2.

Contrary to the argument of the Securities and Exchange Commission (Br. pp. 12, 26), the Arbitration Act affords no room for judicial determination as to whether an issue is referable to arbitration. It is true that Section 3 of the Act prescribes procedure to be followed when an action is commenced "upon any issue referable to arbitration" but that section does not limit Sections 1 and 2 which prescribe that the Act includes all "maritime transactions" and all contracts and transactions involving interstate commerce excepting only "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."

There is no conflict between the provisions of the Arbitration Act and those of the Securities and Exchange Act of 1933. There is nothing in the latter Act which expressly, or by any reasonable implication, repeals, narrows or limits the plain wording of the Arbitration Act. "The essential purpose of the statute is to protect investors by requiring publication of certain information concerning securities before offered for sale." (*A. C. Frost & Co.* v. *Coeur d'Alene Mines Corp.*, 312 U. S. 38, 40 (1941)).

Under the Act, this purpose is effectuated by requiring the seller to comply with certain provisions of the Act and the regulations promulgated under it with respect to the manner of marketing securities and furnishing information.

The provisions of Section 14 of the Securities Act making void any agreement to waive "compliance" with the Act plainly refer to the seller's "compliance" with the substantive provisions of the Act and not to the buyer's remedies when there has been a failure of compliance on the part of the seller.

In any event, however, an agreement between the buyer and seller to refer a dispute to arbitration does not constitute any waiver at all. The Act created a liability on the part of the seller for any damages sustained by the buyer by reason of an untrue statement of a material fact by the seller or the omission to state material facts, unless the seller can sustain the burden of proof that he did not know and "in the exercise of reasonable care could not have known, of such untruth or omission." It was therefore necessary to provide a forum for this new cause of action. Accordingly, the Act provides that the buyer "may sue either at law or in equity in any court of competent jurisdiction" on this new statutory cause of action. The buyer is thus afforded a statutory cause of action in the federal courts irrespective of diversity of citizenship or jurisdictional amount. In conferring the right to sue in any court of competent jurisdiction at law or in equity, the Act does not limit the remedy to any particular mode of trial. Under the Arbitration Act it is implicit that arbitration is merely a form of trial to be adopted in the action itself in place of the trial at common law, just as actions

are tried before referees or special masters instead of judges and juries. Arbitration was a mode of trial in existence when the Securities Act was adopted, and that statute evidences no intention to alter or repeal it.

Under the heading "Arbitration Cannot Assure the Customer His Statutory Rights" (Br. pp. 30-44) the brief of the Commission marshalls various quotations from texts dealing with the subject of arbitration to suggest that arbitration is of limited value and peculiarly suited to certain limited types of controversies, but this is an argument against the efficacy of arbitration itself—foreclosed by the policy already expressed by Congress in the Federal Arbitration Act.

In urging the informality of the arbitration procedure as a ground for its rejection here, the Commission ignores the fact that arbitrators as a matter of law can decide only the specific controversy referred to them; that the Court of Appeals here has held that the controversy to be submitted to arbitration here shall be that arising under the Securities Act of 1933 including, specifically, the burden imposed by the Act, upon the broker to prove, if there was any misstatement, that he did not know of it, and reasonably could not have known of it; and that the arbitrators' failure or refusal to decide in accordance with this provision would "constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (48, 49).

The question of law to be decided here is no different than if it were the broker rather than the customer who was trying to escape from his agreement to arbitrate. In

this case, the customer, petitioner, conceives it to be to his interest to go to court rather than to arbitration. In the next case, the situation may well be reversed with the broker resisting arbitration and the customer demanding it. In either case, the question of law is the same.

It is suggested by the Commission (Br. pp. 14, 44) that what is called a "post-controversy" agreement of arbitration would be permissible even though a pre-controversy agreement is contended to be invalid. The Arbitration Act, in Section 2, expressly puts pre-controversy and post-controversy arbitration agreements on precisely the same footing. It validates agreements to arbitrate either "a controversy thereafter arising" or "an existing controversy." The suggestion made therefore would be judicial legislation in its purest form for there is utterly no expression by Congress evidencing any intention to differentiate between them. The very making of the suggestion exposes petitioner's position for what it really is—an attempt to induce this Court to enact legislation which Congress has not.

There is no conflict at all between the two statutes and the decision below properly gives full force and effect to the policies established by Congress in both—allowing both to stand, side by side, with neither encroaching on the other. It affords full recognition and enforcement of rights and liabilities under the Securities Act of 1933. At the same time, it preserves to all parties the right afforded them by the 1925 Act to contract to have those rights and liabilities enforced in the trial forum of their choice, arbitration, without assuming to read into the later enactment provisions which Congress itself neither expressed nor

implied. There is no conflict between the two Acts, or between their respective policies, provisions or objectives.

Throughout the Commission's brief there is constant reiteration of the statement that the arbitration provision, while admittedly appearing directly above the customer's signature, is contained in "a fine-print pre-transaction agreement." Such statements are prefaced, on page 8, with the comment that there "is no indication in the record that the various provisions of the agreement were actually read by the petitioner, or explained to him, before his signature was obtained." There is no indication in the record to the contrary. The record is silent on the subject. Moreover, this is utterly irrelevant to the issue before this Court. The Arbitration Act, by Section 2, specifically preserves to petitioner his rights "upon such grounds as exist at law or in equity for the revocation" of his contract. He is therefore fully protected if he claims the contract to be unenforceable because of fraud, misrepresentation, duress, or for any legitimate reason. When respondent moved here for a stay petitioner made no such claim. Instead, he filed no affidavit at all, but merely contested respondents' motion as a matter of law. From this, as the Court of Appeals observed, "we must assume that the plaintiff [petitioner] voluntarily entered into the agreement and fully understood its terms" (43). The Commission's speculations and its comments upon the size of the type are thoroughly unwarranted in the light of petitioner's own conduct and the language of the statute which afforded him full protection had he chosen to make any such claim himself.

Preservation in securities transactions of the speedy remedy of arbitration, voluntarily selected by the parties, is of great importance in the light of the large volume of such business done in New York City, where delay due to calendar congestion in both state and federal courts is notorious. In the absence of a clear expression from Congress, the Arbitration Act should not be thus foreshortened.

POINT I

The Provisions and Policy of the Securities Act of 1933 Do Not Forbid Arbitration as a Mode of Settling Disputes Arising from an Alleged Violation of Section 12(2) Thereof.

At the outset, we must recognize the "cardinal principle of construction that repeals by implication are not favored. When there are two acts upon the same subject, the rule is to give effect to both if possible." *United States* v. *Borden Co.*, 308 U. S. 188, 198 (1939). See *United States Alkali Export Ass'n* v. *United States*, 325 U. S. 196, 206 (1945). The policy which Congress recognized and favored in 1925 was at least as strong and valid in 1951, when petitioner signed the margin agreement in issue. That Congress happened to recognize and further a policy of another type in 1933, when it passed the Securities Act, cannot affect the 1925 Act in the absence of a clear showing of conflict between the two policies.

The principles of the securities legislation as outlined in the President's message to Congress of March 29, 1933 were summarized thus in H. R. Rep. No. 85, 73d Cong., 1st Sess. 3 (1933):

"* * * In brief, the aims set forth by the President are:

(1) An insistence that there should be full disclosure of every essentially important element attending the issue of a new security.

(2) A requirement that whatever action taken by the Federal Government for such disclosure should be limited to that purpose and should be so devised as not to be capable of being construed as an approval or guarantee of a security issue.

(3) A demand that the persons, whether they be directors, experts, or underwriters, who sponsor the investment of other people's money should be held up to the high standards of trusteeship.

The achievement of these ends is the principal purpose of this bill."

The policy of the Federal Arbitration Act was expressed by the House Judiciary Committee as follows:

"The purpose of this bill is to make valid and enforcible agreements for arbitration contained in contracts involving interstate commerce or within the jurisdiction or [sic] admiralty, or which may be the subject of litigation in the Federal courts. It was drafted by a committee of the American Bar Association and is sponsored by that association and by a large number of trade bodies whose representatives appeared before the committee on the hearing. There was no opposition to the bill before the committee.

* * *

"Arbitration agreements are purely matters of contract, and the effect of the bill is simply to make the contracting party live up to his agreement. He

can no longer refuse to perform his contract when it becomes disadvantageous to him. An arbitration agreement is placed upon the same footing as other contracts, where it belongs.

"The need for the law arises from an anachronism of our American law. Some centuries ago, because of the jealousy of the English courts for their own jurisdiction, they refused to enforce specific agreements to arbitrate upon the ground that the courts were thereby ousted from their jurisdiction. This jealousy survived for so lon [sic] a period that the principle became firmly embedded in the English common law and was adopted with it by the American courts. The courts have felt that the precedent was too strongly fixed to be overturned without legislative enactment, although they have frequently criticized the rule and recognized its illogical nature and the injustice which results from it. The bill declares simply that such agreements for arbitration shall be enforced, and provides a procedure in the Federal courts for their enforcement.

* * *

"In view of the strong support of commercial and legal bodies, the entire lack of opposition before the committee, the obvious justice of the result sought to be attained, and the evident propriety and necessity of Federal action, we submit that the bill should become law. It is practically appropriate that the action should be taken at this time when there is so much agitation against the costliness and delays of litigation. These matters can be largely eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable."

H. R. Rep. No. 96, 68 Cong., 1st Sess. 1-2 (1924).

The Senate committee said:

> "It has been said that 'arrangements for avoiding the delay and expense of litigation and referring a dispute to friends or neutral persons are a natural practice of which traces may be found in any state of society.' The desire to avoid the delay and expense of litigation persists. The desire grows with time and as delays and expenses increase. The settlement of disputes by arbitration appeals to big business and little business alike, to corporate interests as well as to individuals.
>
> • • •
>
> "The bill, while relating to maritime transactions and to contracts in interstate and foreign commerce, follows the lines of the New York arbitration law enacted in 1920, amended in 1921, and sustained by the decision of the Supreme Court of the United States in the matter of the Red Cross Line v. Atlantic Fruit Co., rendered February 18, 1924."
>
> Sen. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924).

In the face of this, there clearly is no conflict of policy. Nor is there any conflict in the provisions.

The Securities Act imposes upon issuers and sellers of securities certain requirements. Thus, registration statements and prospectuses must contain certain information specified in the Act. Sections 6, 7, and 10, 15 U. S. C. §§77f, 77g, and 77j. These documents are to be filed in the manner and within the times stated. Section 8, 15 U. S. C. §77h. Nor may a seller include an untrue statement or omit a material fact the omission of which might be misleading. Section 12(2), 15 U. S. C. §77*l* (2). With all these require-

ments the broker selling securities must comply. Waiver of compliance is void. Section 14, 15 U. S. C. §77n.

The plain meaning of Section 14 is that the broker cannot secure immunity for himself from complying with the burdens imposed upon him by any agreement with, or waiver by, his customer. The term "compliance with" can only be satisfied by the broker. It is he who must comply with the Act. No duties of compliance whatever are placed upon the customer. Illustrative of a waiver of compliance with the provisions of the Act would be clauses waiving the requirements of a registration statement, or for the delivery of a prospectus or some of the essential items of information listed in the statute. Any waiver of liability for making untrue statements or attempts to shift the burden of proof would be in the same category.

It is plain that the words "waive compliance with any provision" are not the same as "to waive the remedies provided by the Securities Act."

Section 14 makes no mention of waiver of remedies. It does not purport to deal with remedies at all. This is not surprising because good draftsmanship would dictate that separate sections deal with remedies for breach. In fact only in the event of non-compliance with some provision of the Act would the occasion arise for any remedy.

In any event, the Commission's whole argument is predicated upon the proposition that an arbitration agreement is a "waiver" of the right to a suit "at law or in equity." But it is no such thing. It is merely an agreement, made enforceable by statute, as to how any controversy will be procedurally determined at law or in

equity. Here petitioner commenced his suit at law in the Southern District of New York. Respondents invoked Section 3 of the Arbitration Act which prescribes the procedure to be followed thereafter in any such suit where it is made to appear that the parties have agreed to arbitrate the controversy involved—a stay, not a dismissal of the suit: "If any suit * * * be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing * * * the court * * * shall * * * stay the trial of the action until such arbitration has been had * * *." The action is not dismissed. It remains pending. Only the trial is stayed. Instead of proceeding to common law trial it is tried before arbitrators, just as other cases are tried before referees or special masters instead of judges and juries. And the award subsequently made by the arbitrators remains subject to review and vacation by the court in the still pending action.

The realities of the situation were explained by Judge Learned Hand in *Murray Oil Products Co.* v. *Mitsui & Co.*, 146 F. 2d 381, 383 (2d Cir. 1944):

> "In either view therefore § 3 did not need to remove, and did not remove, what would at common law have been a bar; on the contrary, it provided the defendant with relief—a stay—under conditions where before he would have been helpless to assert the arbitration clause at all. This was the measure of its change, so far as we can see; had it meant to go further and finally to dispose of the action, as the defendant argues, it would not have chosen the words used, for a stay presupposes that the action shall not abate; and if it does not, it must go to judgment of one kind or another. If a defendant wins before

> the arbitrators, he must be able to clinch his victory by a judgment; on the other hand, having invoked arbitration, he must also abide the result, if he loses. It would be a lame and impotent conclusion in that event to require the successful plaintiff to begin a new action on the award. Arbitration is merely a form of trial, to be adopted in the action itself, in place of the trial at common law: it is like a reference to a master, or an 'advisory trial' under Federal Rules of Civil Procedure, Rule 39(c), 28 U.S.C.A. following section 723c. That is the whole effect of §3."

In 1925, Congress, by the Arbitration Act, imported into suits at law or in equity the procedure to be followed in such suits where an arbitration agreement existed. It is not a defense or ground of dismissal of the suit. As Judge Hand said, it is merely the prescribed "form of trial, to be adopted in the action itself, in place of the trial at common law."

It is not therefore in any sense a "waiver" of the right to sue at law or in equity—it is only an agreement, sanctioned by Congress, as to the procedure to be followed in the conduct of such suits.

Thus, the whole basis for the Commission's argument (Br. pp. 19-20) falls. Whatever might be the effect if all remedies were waived, it is plain here that there is no waiver at all.

Plainly, too, the permissive words of Section 12(2) of the Act—that, upon non-compliance by the seller, the purchaser "may sue either at law or in equity"—are not mandatory and do not forbid him to seek his damages in

any other manner—such as by settlement or by arbitration. Laws governing venue and jurisdiction, even when apparently affording exclusive jurisdiction to the courts, do not inhibit arbitration.

In *Cavicchi* v. *Mohawk Manufacturing Co.*, 308 U. S. 522 (1939), this Court had before it the policy of the Judicial Code (now 28 U. S. C. §1338), which provided that the jurisdiction of the United States courts should "be exclusive of the courts of the several States * * *" in "all cases arising under the patent-right * * * laws of the United States." A dispute arose as to the validity of a patent, and the parties agreed to submit the dispute to arbitration. The arbitration resulted in an award, which was confirmed under New York law in a state court. The New York Court of Appeals affirmed the order confirming the award, holding that arbitration did not offend the quoted language of the Judicial Code. *Matter of Mohawk Manufacturing Co.* v. *Cavicchi*, 281 N. Y. 629, 22 N. E. 2d 179 (1939). This Court dismissed an appeal for want of a substantial federal question, citing *Red Cross Line* v. *Atlantic Fruit Co.*, 264 U. S. 109 (1924). In the *Red Cross Line* case this Court was urged to vindicate the policy requiring state and federal courts to apply admiralty law uniformly, the requirement of uniformity being implied from the Constitution itself. The New York court had required arbitration of a contract cognizable in admiralty at a time when the federal courts sitting in admiralty would have refused arbitration. This Court held that the policy requiring uniformity in admiralty law was not so all-embracing as to forbid a state from devising its own procedures.

for enforcement of rights, as long as it adhered to the substantive federal law.

At p. 27 the Commission cites a contrary holding in 1930 by the Delaware district court in *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184. Plainly, this case can no longer be regarded as binding. See Robb, *Arbitration Procedure Compared with Court Litigation in Patent Controversies*, 17 Law and Contemp. Prob. 679, 690-1, 693 (1952).

In addition to excluding employment contracts from the scope of federal arbitration, Congress specifically provided in Section 8, 9 U. S. C. §8, that arbitration in admiralty should not prevent "the party claiming to be aggrieved" from beginning "his proceeding hereunder by libel and seizure of the vessel * * *." In *The Anaconda* v. *American Sugar Refining Co.*, 322 U. S. 42 (1944), the owner of a vessel had required of the company to which it was being chartered an arbitration agreement with a clause rendering Section 8 of the Act inapplicable. When a suit between the parties was commenced by a libel against the vessel, the charterer interposed this clause as a defense. This Court held it invalid, 322 U. S. at 46:

> "* * * Congress plainly and emphatically declared that although the parties had agreed to arbitrate, the traditional admiralty procedure with its concomitant security should be available to the aggrieved party without in any way lessening his obligation to arbitrate his grievance rather than litigate the merits in court.
>
> "It is enough that Congress had so declared. We think a party can not stipulate away such a

jurisdiction which the legislation declares open as heretofore."

Clearly, in a statute whose metes and bounds have been so plainly delineated by Congress, there is no room for further drastic limitation by judicial construction of provisions constituting merely a grant of jurisdiction and a broadening of venue.

The Courts of Appeal recognize that provisions in other statutes, even where couched in far more mandatory language than here, are permissive only and do not preclude arbitration.

In the Fair Labor Standards Act (29 U. S. C. §201 *et seq.*) a special statutory penalty was imposed with the provision that an action to recover such liability "may be maintained in any court of competent jurisdiction * * *." The statutory grant of the privilege to resort to any court of competent jurisdiction is identical with that specified in the Securities Act.

The Court of Appeals for the Third Circuit in *Donahue v. Susquehanna Collieries Co.*, 138 F. 2d 3 (3d Cir. 1943), had to deal with a situation almost parallel with that now presented to this Court. There a motion for a stay of trial pending arbitration in accordance with Section 3 of the Federal Arbitration Act was made. There, as here, it was argued that special rights were created by statute which would not lend themselves to arbitration. The court granted the motion for a stay pending arbitration and in its opinion succinctly answered the objections made, saying:

> "Is there anything about the Fair Labor Standards Act which removes claims under its terms

from the arbitration clause? We may concede that Congress could have done so had it wished. It could have provided that any claim under the Act was to be enforced by lawsuit only, notwithstanding any agreement between parties for any other method of settlement. There is no such express language. The plaintiff points to a sentence in the section on 'Penalties; civil and criminal liability' which he contends has the effect just described. 'Action to recover such liability may be maintained in any court of competent jurisdiction * * *' is the language used. We think the effect of this provision is to allow a suitor to proceed in federal court regardless of citizenship of the litigants and amount involved or to sue in a state court at his convenience" (138 F. 2d, at p. 6).

* * *

"No doubt it creates rights which made a basis of a claim by an employee against an employer who violates it. So does any contract. A claim under the Act and a claim based on a contract,—each is based on a legal right which the claimant asserts against someone else. Arbitration is one way by which such a right can be enforced" (138 F. 2d 3, at p. 6).

In *Agostini Bros. Building Corp.* v. *United States*, 142 F. 2d 854 (4th Cir. 1944), an action was brought under the Miller Act (40 U. S. C. §§270a-270d) to recover for labor and materials furnished in the construction of a public building. The defendants sought to stay the federal court action until arbitration could be had pursuant to the terms of the contract. The District Court denied the motion but the Court of Appeals unanimously reversed and directed a stay pend-

ing arbitration. There the statute creating the rights was far more directive than the Securities Act because it prescribed:

> "(b) *Every suit instituted under this section shall* be brought in the name of the United States for the use of the person suing, in the United States District Court for any district in which the contract was to be performed and executed *and not elsewhere,* irrespective of the amount in controversy * * *" (40 U. S. C. §270b (b)) [Emphasis supplied].

Despite this direction, the stay pending arbitration was granted.

In *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (3d Cir. 1945), cert. denied, 327 U. S. 777 (1946), the Court of Appeals held that an action by employees to recover unpaid overtime wages, liquidated damages, reasonable attorneys' fees and court costs under Section 16 of the Fair Labor Standards Act of 1938 (29 U. S. C. §216) was subject to arbitration. In that case the Wage and Hour Division of the United States Department of Labor appeared *amicus curiae,* as the Securities and Exchange Commission has done in the case at bar to urge that arbitration was not applicable. Nevertheless, the court stayed the action pending arbitration.

There is thus nothing in the Act—either in the non-waiver provision or the remedies provision—which expressly or by any reasonable implication can be said to preclude arbitration.

The situation is entirely different from that in *Boyd* v. *Grand Trunk Western Railroad Co.*, 338 U. S. 263 (1949), upon which the Commission relies (Br. pp. 20-22). There

the Act gave the employee a wide choice of venue which, as the Commission concedes, was designed to enable him to pick his jurisdiction so as to include large cities where the amount of his jury verdict would probably be larger. The statute prohibited the carrier from exempting itself "from any liability created by this Act." Federal Employers' Liability Act Section 5, 45 U. S. C. §55. In that case the court could readily take notice on the basis of judicial experience that a waiver of venue could so affect the extent of liability as to constitute a waiver of liability. Apart from the fact that there is no waiver of liability involved here, there would be no reasonable basis for a supposition that arbitration as a mode of trial in this action would affect liability.

Brooklyn Savings Bank v. *O'Neil*, 324 U. S. 697 (1945), is likewise not applicable. The holding there was that an attempted release of the liquidated damages provided for under the Fair Labor Standards Act was invalid because, as Mr. Justice Reed pointed out, ". . . the legislative policy would be thwarted by permitting such contracts." 324 U. S. at 713. The case did not involve a question of statutory construction of either a waiver provision or an arbitration clause.

The fears expressed below and by the Commission (Br. p. 30 *et seq.*) that the burden of proof and other provisions of the Act will not be honored in arbitration, involving as it does a challenge to the integrity and good faith of as yet unchosen arbitrators, reflects to an extent a failure fully to "shake off the old judicial hostility to arbitration," *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F.

2d 978, 985 (2d Cir. 1942). In any event, there is no reason to suppose that arbitration here would be in any way weighted against petitioner. Constant assertion is made that, if arbitration be sustained, petitioner's rights will not be upheld by arbitrators taken from "an industry selected panel." By this the Commission assumes that members of the securities industry, even after they have done business for 20 years under the Securities Act, must necessarily be presumed hostile to it. More importantly it ignores the fact that under the arbitration provision the petitioner himself is given the right to have his claims arbitrated by arbitrators selected from other than the New York Stock Exchange panel. The provision specifically allows petitioner to select either the New York Chamber of Commerce, the American Arbitration Association, or the New York Stock Exchange arbitration rules (16, 22). The American Arbitration Association, for example, favors a lawyer as one of a panel whenever there are, as here, three arbitrators to act. Note, *Predictability of Result in Commercial Arbitration*, 61 Harv. L. Rev. 1022, 1023 n. 12 (1948).

The brief of the Commission (p. 13) asserts:

> "The arbitration process is primarily suited for commercial disputes which often can best be resolved by businessmen on the basis of their own knowledge and experience, and without reference to technical rules of law."

It is suggested (Br. pp. 31, 32) that it is a remedy peculiarly adapted to the disposition of disputes between merchants; that in the securities field it may be a means for settling a variety of technical business disputes; but that where expertise in the law rather than experience in a par-

ticular phase of business is essential to a proper determination of the particular controversy, the arbitration process may be fraught with danger. There is no foundation in fact for these expressions of opinion.

Arbitration has been widely and satisfactorily employed entirely outside the commercial field.

It is a matter of common knowledge that the labor unions have insisted upon and obtained in a great number of major collective bargaining agreements provisions for the compulsory settlement of disputes by arbitration—a plain indication that labor does not feel that arbitration is weighted in favor of business or that its usefulness is confined to commercial disputes. See also 61 Harv. L. Rev. 1027, where the author found it necessary to dispute the contention that arbitration is favorable to the "little man" and 61 Harv. L. Rev. 1031 where it is intimated that in landlord and tenant cases the arbitrators are unduly favorable to tenants rather than landlords.

Finally, the District Court would not confirm an award where the arbitrators are shown to have been actually or potentially biased. See *Stathatos* v. *Arnold Bernstein S. S. Corp.*, 202 F. 2d 525, 526 (2d Cir. 1953); *Petrol Corporation* v. *Groupement d'Achat des Carburants*, 84 F. Supp. 446, 447 (S. D. N. Y. 1949); cf. *Lipschutz* v. *Gutwirth*, 304 N. Y. 58, 106 N. E. 2d 8 (1952).

Arbitrators can readily be requested to follow legal rules. Indeed, in England the arbitrators must decide "according to the legal rights of the parties" (48 n. 9). *Jager* v. *Tolme & Runge*, [1916] 1 K. B. 939, 953 (C. A.); *Czarnikow* v. *Roth, Schmidt & Co.*, [1922] 2 K. B. 478, 484 (C. A.); *Stotesbury* v. *Turner*, [1943] K. B. 370.

What Lord Justice Bankes said in the *Czarnikow* case is apposite. He said, [1922] 2 K. B. at 484:

> "Among commercial men what are commonly called commercial arbitrations are undoubtedly and deservedly popular. That they will continue their present popularity I entertain no doubt, so long as the law retains sufficient hold over them to prevent and redress any injustice on the part of the arbitrator, and to secure that the law that is administered by an arbitrator is in substance the law of the land and not some home-made law of the particular arbitrator or the particular association. To release real and effective control over commercial arbitrations is to allow the arbitrator, or the Arbitration Tribunal, to be a law unto himself, or themselves, to give him or them a free hand to decide according to law or not according to law. • • • Unlimited power does not conduce to reasonableness of view or conduct."

The Commission seeks to weaken the effect of the English cases by asserting (Br. p. 29) that even apart from statute the English courts had refused to enforce arbitration of fraud cases. The authorities cited (Br. p. 29 n. 20) for this proposition do not support it. Both the *Wallis* and *Workman* cases cited are holdings only that the particular controversies involved did not come within the scope of the arbitration agreement as written. There is some language in the *Workman* case in regard to the effect of fraud but it clearly does not stand for the broad proposition for which it is cited by the Commission. The *Green* case involved an election of remedies where the party seeking arbitration had gone to court instead of requesting arbitration within a three day limitation provided for in the agreement. In

any event, the cases would not be in point because under the law of England as it stood when they were decided, the English courts, unlike our courts under the Arbitration Act, had discretion as to whether to stay proceedings pending arbitration. Thus in the *Barnes* case, cited in the Commission's footnote, the Court said, [1898] 1 Ch. at 417:

> "In matters of this kind—motions to stay proceedings by reason of an agreement to refer to arbitration—the Court undoubtedly has a discretion—a judicial discretion of course. In the present case, looking at the circumstances, I think in exercising my judicial discretion I ought not to order a stay of proceedings."

At Br. p. 36, the Commission refers to certain provisions of the English Arbitration Act under which the court at the request of the arbitrator can make rulings on questions of law during the course of the arbitration. The same result has already been obtained here. Under the ruling below the arbitrators are required to determine, if any misstatements of fact were made by the seller, whether the seller can sustain the burden of proving that it did not know and could not in the exercise of reasonable care have known of the misstatements. In other words, here the Court has already ruled and laid down the principles of law which must and will govern the arbitration.

We know of no case in this country which holds that arbitrators may not be required, by the terms of the submission, to follow legal standards. On the contrary, there are many instances of arbitrators being required to decide in accordance with a specific statute or in accordance with

a standard set forth in the submission agreement. *Campbell* v. *American Fabrics Co.*, 168 F. 2d 959, 962 (2d Cir. 1948); *Evans* v. *Hudson Coal Co.*, 165 F. 2d 970, 974 (3d Cir. 1948); *Columbian Fuel Corporation* v. *United Fuel Gas Co.*, 72 F. Supp. 843, 844-45 (S. D. W. Va. 1947), aff'd, 165 F. 2d 746 (4th Cir. 1948); *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311, 313, 321 (3d Cir. 1945), cert. denied, 327 U. S. 777 (1946); *Toledo S. S. Co.* v. *Zenith Transp. Co.*, 184 Fed. 391, 392, 395 (6th Cir. 1911). ". . . whether the arbitrator shall hear the case according to rules of the law of evidence and/or according to substantive law, depends upon the agreement of the parties; they may agree that one or more of those rules shall apply." Dean Wesley A. Sturges, address before the Association of the Bar of the City of New York (74 Reports, Association of the Bar, 1941).

Judge Goodrich was blunt on this point in *Watkins* v. *Hudson Coal Co.*, where he ruled, 151 F. 2d at 313:

> "Our conclusion is that the matter should proceed to arbitration, but only in accordance with the rulings of law as hereinafter set out."

The New York courts consider it a matter of course that arbitrators must decide in accordance with law if the submission so provides. See *Matter of Springs Cotton Mills (Buster Boy Suit Co.)*, 275 App. Div. 196, 200, 88 N. Y. S. 2d 295 (1st Dep't), aff'd, 300 N. Y. 586, 89 N. E. 2d 877 (1949); cf. *Tarello* v. *John A. Johnson Contracting Corporation*, 50 N. Y. S. 2d 212 (not officially reported) (Sup. Ct.), aff'd, 268 App. Div. 893, 51 N. Y. S. 2d 87, leave to appeal denied, 268 App. Div. 903, 51 N. Y. S. 2d 640 (1st Dep't 1944), 294 N. Y. 646, 68 N. E. 2d 523 (1945).

As a matter of fact, such evidence as there is indicates that arbitrators tend to follow the law. The *Harvard Law Review* studied about 300 unpublished decisions under the rules of the American Arbitration Association rendered from October 1946 through December 1947, and reached this conclusion, Note, *Predictability of Result in Commercial Arbitration*, 61 Harv. L. Rev. 1022, 1024 (1948):

> "The awards of arbitrators show rather close adherence to the rules of substantive law insofar as law can be isolated from fact or procedure. This is clearly so where the ethical notions underlying such rules appeal to a layman. No one need explain to an arbitrator the social utility of enforcing contractual obligations, in order to convince the arbitrator that a breach of contract should be compensated. But where the ethical notions underlying rules of law have little or no appeal in a particular business context, arbitrators may disregard the legal rule. Consequently the lawyer must test the 'law' applicable to the case by his knowledge of business ethics and trade custom. This leaves for the lawyer the task of determining when the moral basis of the applicable law is too weak to compete with ethical business notions not relevant in a court. But this is a far cry from saying that anything can happen in arbitration."

Nor is there any basis for holding that the underlying policy of the Act, or the nature of the arbitration process, requires any different conclusion.

In enacting the Securities Act, Congress was not dealing with arbitration but with the evils created by the failure to give accurate or adequate information to the purchaser

of securities. There was no finding or even supposition that the public had failed to receive proper redress from sellers of securities because of arbitration or arbitration agreements. In all the investigations by congressional committees of fraudulent and deceptive practices to which purchasers of securities were subject (see, *e.g.*, *Stock Exchange Practices*, Sen. Rep. No. 1455, 73d Cong., 2d Sess. 5-81 (1934)), there is no showing that arbitration agreements had been used or were even thought of as instruments of oppression. No facts were presented and there was no debate upon the subject tending to show that claims arising from misrepresentation of facts in connection with security transactions must be brought exclusively in the courts and the parties deprived of recourse to any other forum.

When Congress passed the Securities Act, the Arbitration Act had been in existence for eight years and provided, where the parties had agreed upon arbitration, for a stay pending arbitration. By 1933 many of the states had passed arbitration statutes and the courts had sustained arbitration agreements. This being the situation, had Congress wished to take away all rights of arbitration with respect to security transactions it would have been a simple matter so to provide. But Congress made no such provision.

We have pointed out at the outset the manifest error underlying the Commission's whole argument (Br. p. 26 *et seq.*) which is predicated upon a misconception of the language contained in Section 3 of the Arbitration Act. The scope of the statute is defined by Sections 1 and 2 and is all inclusive, except for employment contracts.

The cases cited in further support of the argument are likewise inapposite. As we have shown, the *Zip* case, cited on page 27, is no longer the law since this Court's decision in the *Cavicchi* case, *supra* p. 19. *Matter of Kingswood Management Corp.* (*Salzman*), 272 App. Div. 328, 70 N. Y. S. 2d 692 (1st Dep't 1947), involved a cause of action for treble damages for overcharges of rent made actionable by the Federal Emergency Price Control Act of 1942 which had been settled by stipulation and entry of judgment in the Municipal Court. This stipulation provided that the matter of attorney's fees should be arbitrated. The Court ruled that since the right to recover attorney's fees was created by a provision of the Act allowing "reasonable attorney's fees and costs *as determined by the court*" (emphasis supplied), any such award must be made by the court which heard the case and which was, therefore, "in the best position to appraise the value of the attorney's services" (272 App. Div. at 330). The Court emphasized that:

> "Power to determine the attorney's fee is incidental to the determination of the action, and can only be exercised in the forum which has jurisdiction thereof" (*id.* at 331).

The statutory remedy in the *Kingswood* case, in terms extending only to fees determined by the same court that heard the treble damage action, was thus quite different from the statutory remedy provided by Section 12(2) of the Securities Act of 1933 (15 U. S. C. §77*l*(2)). Beyond the provision that the person damaged might sue either at law or in equity in any court of competent jurisdiction, there is nothing in the substantive language of that section mak-

ing the determination of the issue one peculiarly within the province of any single court.

In *Application of Diamond*, 80 N. Y. S. 2d 465 (not officially reported) (Sup. Ct.), aff'd, 274 App. Div. 762, 79 N. Y. S. 2d 924 (1st Dep't 1948), the decision merely was that in a stockholder's derivative suit an arbitration agreement contained in a contract between the corporation's stockholders was inapplicable to the controversy involved. *Application of Cohen*, 183 Misc. 1034, 52 N. Y. S. 2d 671 (Sup. Ct. 1944), aff'd, 269 App. Div. 663, 53 N. Y. S. 2d 467 (1st Dep't 1945), leave to appeal denied, 269 App. Div. 690, 54 N. Y. S. 2d 389, 294 N. Y. 640, 61 N. E. 2d 459 (1945), involved a construction of an arbitration agreement between the stockholders providing for arbitration of controversies involving "the conduct of the business." The Court held that this agreement plainly did not apply in a statutory proceeding for dissolution of the corporation where the stockholders were deadlocked. Obviously, the sovereign right of control, and its governmental interest in, the matter of custody of children and the distribution of decedents' estates would forbid such matters' being relegated to private arbitration, which was all that was held in *Hill* v. *Hill*, 199 Misc. 1035, 104 N. Y. S. 2d 755 (Sup. Ct. 1951), and *Swislocki* v. *Spiewak*, 273 App. Div. 768, 75 N. Y. S. 2d 147 (1st Dep't 1947). The *Quarrington Court* case, Br. p. 28, 102 F. 2d 916 (2d Cir.), cert. denied, 307 U. S. 645 (1939), merely held that a ship owner could not seek piecemeal determination by arbitration with one of several parties involved in a plenary limitation proceeding which he himself had commenced joining all interested parties.

There is, on the face of the statute and the existing authorities, no basis therefore for selecting any kind of contracts or transactions as being outside the scope of the Arbitration Act where, as here, Congress has given no indication whatever that such was its intention.

CONCLUSION

The judgment below should be affirmed.

Respectfully submitted,

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